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AUTHORITY: 5 U.S.C. App. 3, 42 U.S.C. 2996e, 2996f, 2996g, 2996h(c)(1), and 2996i(c); Pub. L. 105-119, 111 Stat. 2440; Pub. L. 104-134, 110 Stat. 3009.

SOURCE: 62 FR 68224, Dec. 31, 1997, unless otherwise noted.

§ 1630.1 Purpose.

This part is intended to provide uniform standards for allowability of costs and to provide a comprehensive, fair, timely, and flexible process for the resolution of questioned costs.

§ 1630.2 Definitions.

(a) *Allowed costs* means a questioned cost that the Corporation, in a management decision, has determined to be eligible for payment from a recipient's Corporation funds.

(b) *Corrective action* means action taken by a recipient that:

- (1) Corrects identified deficiencies;
- (2) Produces recommended improvements; or
- (3) Demonstrates that audit or other findings are either invalid or do not warrant recipient action.

(c) *Derivative income* means income earned by a recipient from Corporation-supported activities during the term of a Corporation grant or contract, and includes, but is not limited to, income from fees for services (including attorney fee awards and reimbursed costs), sales and rentals of real or personal property, and interest earned on Corporation grant or contract advances.

(d) *Disallowed cost* means a questioned cost that the Corporation, in a management decision, has determined should not be charged to a recipient's Corporation funds.

(e) *Final action* means the completion of all actions that Corporation management, in a management decision, has concluded are necessary with respect to the findings and recommendations in an audit or other report. In the event that Corporation management concludes no corrective action is nec-

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essary, final action occurs when a management decision has been made.

(f) *Management decision* means the evaluation by Corporation management of findings and recommendations in an audit or other report and the recipient's response to the report, and the issuance of a final, written decision by management concerning its response to such findings and recommendations, including any corrective actions which Corporation management has concluded are necessary to address the findings and recommendations.

(g) *Questioned cost* means a cost that a recipient has charged to Corporation funds which Corporation management, the Office of Inspector General, the General Accounting Office, or an independent auditor or other audit organization authorized to conduct an audit of a recipient has questioned because of an audit or other finding that:

(1) There may have been a violation of a provision of a law, regulation, contract, grant, or other agreement or document governing the use of Corporation funds;

(2) The cost is not supported by adequate documentation; or

(3) The cost incurred appears unnecessary or unreasonable and does not reflect the actions a prudent person would take in the circumstances.

(h) *Recipient* as used in this part means any grantee or contractor receiving funds from the Corporation under sections 1006(a)(1) or 1006(a)(3) of the Act.

[62 FR 68225, Dec. 31, 1997; 63 FR 1532, Jan. 9, 1998]

§ 1630.3 Standards governing allowability of costs under Corporation grants or contracts.

(a) *General criteria.* Expenditures by a recipient are allowable under the recipient's grant or contract only if the recipient can demonstrate that the cost was:

(1) Actually incurred in the performance of the grant or contract and the recipient was liable for payment;

(2) Reasonable and necessary for the performance of the grant or contract as approved by the Corporation;

(3) Allocable to the grant or contract;

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(4) In compliance with the Act, applicable appropriations law, Corporation rules, regulations, guidelines, and instructions, the Accounting Guide for LSC Recipients, the terms and conditions of the grant or contract, and other applicable law;

(5) Consistent with accounting policies and procedures that apply uniformly to both Corporation-financed and other activities of the recipient;

(6) Accorded consistent treatment over time;

(7) Determined in accordance with generally accepted accounting principles;

(8) Not included as a cost or used to meet cost sharing or matching requirements of any other federally financed program, unless the agency whose funds are being matched determines in writing that Corporation funds may be used for federal matching purposes; and

(9) Adequately and contemporaneously documented in business records accessible during normal business hours to Corporation management, the Office of Inspector General, the General Accounting Office, and independent auditors or other audit organizations authorized to conduct audits of recipients.

(b) *Reasonable costs.* A cost is reasonable if, in its nature or amount, it does not exceed that which would be incurred by a prudent person under the same or similar circumstances prevailing at the time the decision was made to incur the cost. If a questioned cost is disallowed solely on the ground that it is excessive, only the amount that is larger than reasonable shall be disallowed. In determining the reasonableness of a given cost, consideration shall be given to:

(1) Whether the cost is of a type generally recognized as ordinary and necessary for the operation of the recipient or the performance of the grant or contract;

(2) The restraints or requirements imposed by such factors as generally accepted sound business practices, arms-length bargaining, Federal and State laws and regulations, and the terms and conditions of the grant or contract;

(3) Whether the recipient acted with prudence under the circumstances, con-

sidering its responsibilities to its clients and employees, the public at large, the Corporation, and the Federal government; and

(4) Significant deviations from the established practices of the recipient which may unjustifiably increase the grant or contract costs.

(c) *Allocable costs.* A cost is allocable to a particular cost objective, such as a grant, project, service, or other activity, in accordance with the relative benefits received. Costs may be allocated to Corporation funds either as direct or indirect costs according to the provisions of this section. A cost is allocable to a Corporation grant or contract if it is treated consistently with other costs incurred for the same purpose in like circumstances and if it:

(1) Is incurred specifically for the grant or contract;

(2) Benefits both the grant or contract and other work and can be distributed in reasonable proportion to the benefits received; or

(3) Is necessary to the overall operation of the recipient, although a direct relationship to any particular cost objective cannot be shown.

(d) *Direct costs.* Direct costs are those that can be identified specifically with a particular final cost objective, i.e., a particular grant award, project, service, or other direct activity of an organization. Costs identified specifically with grant awards are direct costs of the awards and are to be assigned directly thereto. Direct costs include, but are not limited to, the salaries and wages of recipient staff who are working on cases or matters that are identified with specific grants or contracts. Salary and wages charged directly to Corporation grants and contracts must be supported by personnel activity reports.

(e) *Indirect costs.* Indirect costs are those that have been incurred for common or joint objectives and cannot be readily identified with a particular final cost objective. Any direct cost of a minor amount may be treated as an indirect cost for reasons of practicality where the accounting treatment for such cost is consistently applied to all final cost objectives. Indirect costs include, but are not limited to, the costs of operating and maintaining facilities,

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and the costs of general program administration, such as the salaries and wages of program staff whose time is not directly attributable to a particular grant or contract. Such staff may include, but are not limited to, executive officers and personnel, accounting, secretarial and clerical staff.

(f) *Allocation of indirect costs.* Where a recipient has only one major function, i.e., the delivery of legal services to low-income clients, allocation of indirect costs may be by a simplified allocation method, whereby total allowable indirect costs (net of applicable credits) are divided by an equitable distribution base and distributed to individual grant awards accordingly. The distribution base may be total direct costs, direct salaries and wages, attorney hours, numbers of cases, numbers of employees, or another base which results in an equitable distribution of indirect costs among funding sources.

(g) *Exception for certain indirect costs.* Some funding sources may refuse to allow the allocation of certain indirect costs to an award. In such instances, a recipient may allocate a proportional share of another funding source's share of an indirect cost to Corporation funds, provided that the activity associated with the indirect cost is permissible under the LSC Act and regulations.

(h) *Applicable credits.* Applicable credits are those receipts or reductions of expenditures which operate to offset or reduce expense items that are allocable to grant awards as direct or indirect costs. Applicable credits include, but are not limited to, purchase discounts, rebates or allowances, recoveries or indemnities on losses, insurance refunds, and adjustments of overpayments or erroneous charges. To the extent that such credits relate to allowable costs, they shall be credited as a cost reduction or cash refund in the same fund to which the related costs are charged.

(i) *Guidance.* The Circulars of the Office of Management and Budget shall provide guidance for all allowable cost questions arising under this part when relevant policies or criteria therein are not inconsistent with the provisions of the Act, applicable appropriations law, this part, the Accounting Guide for LSC Recipients, Corporation rules, reg-

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ulations, guidelines, instructions, and other applicable law.

[62 FR 68225, Dec. 31, 1997; 63 FR 1532, Jan. 9, 1998]

§ 1630.4 Burden of proof.

The recipient shall have the burden of proof under this part.

§ 1630.5 Costs requiring Corporation prior approval.

(a) *Advance understandings.* Under any given grant award, the reasonableness and allocability of certain cost items may be difficult to determine. In order to avoid subsequent disallowance or dispute based on unreasonableness or nonallocability, recipients may seek a written understanding from the Corporation in advance of incurring special or unusual costs. If a recipient elects not to seek an advance understanding from the Corporation, the absence of an advance understanding on any element of a cost does not affect the reasonableness or allocability of the cost.

(b) *Prior approvals.* Without prior written approval of the Corporation, no cost attributable to any of the following may be charged to Corporation funds:

(1) Pre-award costs and costs incurred after the cessation of funding;

(2) Purchases and leases of equipment, furniture, or other personal, non-expendable property, if the current purchase price of any individual item of property exceeds \$10,000;

(3) Purchases of real property; and

(4) Capital expenditures exceeding \$10,000 to improve real property.

(c) *Duration.* The Corporation's approval or advance understanding shall be valid for one year, or for a greater period of time which the Corporation may specify in its approval or understanding.

§ 1630.6 Timetable and basis for granting prior approval.

(a) The Corporation shall grant prior approval of a cost if the recipient has provided sufficient written information to demonstrate that the cost would be